

UPDATE: FOREIGN INVESTMENTS SAFETY ALERT

Overview of limitations of foreign investments and consequences for foreign companies in Russia

16 March 2022

Due to the significant changes of the investment climate in Russia, the Russian Government has introduced a number of extraordinary measures to prevent foreign investor and capital flight, some of them directly targeting multinationals operating in Russia.

On March 7, the Government approved [the list of countries](#), exercising unfriendly actions in relation to Russia (“unfriendly nations”). The list of “unfriendly nations” will become one of the key tools of law enforcement practice in the context of counter-sanction measures, including issues of parallel imports, selective waiver of intellectual property rights, etc. The list includes the US, all EU member-states, UK, Canada, Australia, Republic of Korea as well as other nations which imposed sanctions on Russia.

On March 10, the Government disclosed more details of the procedure for appointing external administration to foreign companies that have decided to stop their activities in Russia, as well as the criteria for introducing external management.

The draft law initiated by the Government may affect enterprises with a foreign participation share of over 25% (direct or indirect ownership by representatives of “unfriendly countries”). External administration can be introduced in two cases:

1. The termination of the entity’s economic activity in Russia (“hard mechanism”).
2. Actions of management bodies that may lead to termination of activities, liquidation and bankruptcy, for example, termination of contracts that is important to keep operations, dismissal of more than one third of the staff, etc. (“soft mechanism”).

On March 15, “United Russia” party (the dominant party in the State Duma) proposed to impose criminal liability for companies that comply with sanctions against Russia inside the country.

Accumulated FDI in Russia constitutes almost 700 billion USD (the majority originating from European Union countries), and their future in Russia represents a significant issue both for the Russian and European economies.

As part of our ongoing efforts to protect and support multinational investments in Russia, Kesarev has prepared a brief guide on the measures introduced by the Government of Russia that affect operations of international companies in the country.

Information will be updated in response to major developments throughout the crisis, with the most recent information highlighted.



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Adopted Legislation / Regulations

Capital flow prevention

Measures to prevent capital control and ensure financial stability are among the top priorities for the Government and the Central Bank. The measures in this area are among the first ones being imposed over the crisis period.

On **February 28**, President Putin signed an [executive order](#) introducing several “response measures” – mainly several capital flow control policies to be enforced since March 1, which will negatively impact Russian investment climate, but may ensure mid-term financial stability, namely:

- Commitment for Russian resident companies to sell 80% of foreign exchange earnings credited from 1 January 2022.
 - The procedure for selling foreign currency will be established by the Central Bank.
- Prohibition for Russian residents to provide foreign loans in foreign currency and credit foreign currency to bank accounts outside of Russia.
- Prohibition of money transfers without opening an electronic payment account provided by foreign suppliers.

Similar measures were previously established by the directive of the Central Bank, however, from a legal point of view, the Presidential Order makes their implementation imperative.

The Central Bank issued [clarifications](#) on implementing that order, saying, among other things, that making foreign currency payments from residents to non-residents to pay for goods or services is not prohibited.



On March 1, President Putin [signed an order on additional temporary measures to ensure financial stability of Russia](#). Key provisions:

- Starting from **March 2**, the following operations of residents with foreign entities linked to “unfriendly states” can be conducted only under a special procedure, i.e., upon a special authorisation: loans and credit operations in roubles, as well as operations with securities and immovable property.
- Starting from March 2, it is prohibited to export foreign currency cash and foreign currency instruments over 10000 USD.

In late February - early March, the Central Bank of Russia banned Russian brokers from fulfilling orders from foreign residents to sell shares of Russian companies. Additionally, foreign individuals and legal entities are prohibited from accruing coupons and dividends of Russian issuers.

On March 9, the Central Bank established a temporary procedure (until September 9) for the money withdrawal from foreign currency deposits or accounts of citizens. It is allowed to cash out up to \$10,000 in foreign currency (any other currency than dollars must be converted into USD at the rate of the Central Bank). Amounts over \$10,000 can be cashed out only in rubles at the rate of the Central Bank on the day of withdrawal.

Counter-sanctions

On March 7, the Government approved [the list of nations](#), exercising unfriendly actions in relation to Russia (“unfriendly nations”). The list currently includes:

- G7 nations
- All EU member-states
- South Korea
- Taiwan
- Switzerland
- Ukraine,
- Etc.

The Government decree was signed to implement a [presidential executive order](#), according to which Russian individuals and legal entities that have foreign currency obligations to foreign lenders from “unfriendly jurisdictions” will be able to pay them in rubles rather than in foreign currency.

At the same time, the list of unfriendly nations will become one of the key tools of law enforcement practice in the context of counter-sanction measures, including import / export restrictions, selective waiver of IP rights, etc.

On March 4 the Russian Parliament adopted [the law](#) to “improve the mechanisms that ensure sustainable economic development in the face of sanctions pressure from foreign states” (*the law was signed by the President on 8 March*). Among other things, this includes (mostly for 2022):



- A possibility of a moratorium on scheduled inspections of SMEs for 2022. Special conditions for conducting state control (oversight) may be introduced by the Government in 2022.
- The Government by a separate legal act may authorize carrying out activities without renewing a license/permit; obtaining licenses/permits and renewing them without obligatory conformity assessment procedures, without paying state fees, without paying for necessary public services; not undergoing conformity assessment procedures for perpetual licenses/permits.
- In terms of public procurement, a possibility to change the essential terms of the contract (subject, price, term, payment procedure, etc.) by decision of the Government, region or municipality is provided. Besides, until December 31, 2022, additional procurement opportunities from a single supplier are provided, while additional cases of cancellation of fines for non-fulfilment of contracts are provided.
- Medical organizations will be able to purchase more products they need according to a simplified procedure (*medicines, consumables, and medical products*).
- Medicines and medical devices that do not have a Russian analogue can be purchased from a single supplier (*if the only manufacturer is not from the country that imposed the sanctions*).
- A special registration procedure is provided in case of medicines deficit due to economic restrictions imposed by other countries.
- The Government may also ban export of medical devices from Russia, previously imported from the countries that imposed economic restrictions.
- To stimulate medicines and medical devices production in Russia, the Government may approve special procedures for the pharmaceutical activity and production licensing.
- Special procedures may be introduced for conformity assessment with technical regulations.
- **The Government is authorized to set a list of products to which IP rights protection cannot be applied.** The list could be approved by a separate Government Decree and poses significant threat to IP rights holders.

On March 6, the Government approved a [decree](#) to amend the methodology for determining the amount of compensation paid to a patent owner when deciding to use an invention, industrial design or utility model without his consent. In relation to patent holders from “unfriendly nations”, the amount of compensation will be set at 0% of the actual proceeds of the person who used the result of intellectual activity (*instead of 0,5% in general*).

The aim of the amendments is to prevent market shortages in the face of foreign companies exits and disruption of supply chains. These measures are intended to mitigate the negative impact on sectors of the economy and enterprises that are largely dependent on foreign technologies, software, etc.

On March 11, it also became known (with reference to the latest version of the Government’s anti-crisis plan) about the possibility of developing and applying a “compulsory licensing” mechanism to some categories of products. The mechanism, first of all, may concern software, as well as other scarce technologies, the list of which must be approved by the Government:

- The mechanism of "compulsory licensing" involves granting the right to use the results of intellectual activity without granting from IP right holder.



- Currently, the Civil Code provides for the possibility of "compulsory licensing" in extreme cases, while providing for compensation to the right holder. The updated mechanism will probably allow not to pay such compensation to right holders from "unfriendly countries".

On March 6, [the Government imposed a temporary ban](#) on the export of medical devices from Russia manufactured in states that "have decided to introduce economic restrictive measures against Russia." Since there is no list of countries that have imposed sanctions on Russia at the legislative level, the list of «unfriendly countries» will probably be used in law enforcement practice.

On March 8, a Presidential [order](#) to approve special economic measures for external trade was published. The order is of framework nature and authorizes the Government to impose a ban on the import and export of certain products or raw materials (*except for goods imported or exported for personal use*). The measures are valid until December 31, 2022.

On March 10, the Government [announced](#) the preparation of a list (not yet available publicly) of goods and equipment which is temporarily prohibited from being exported from the country:

- The list includes more than 200 categories of goods affecting the main areas of production - industry, medicine, telecommunications, agriculture, etc.
- The export of these goods is temporarily restricted to all foreign countries, with the exception of the member states of the Eurasian Economic Union (EAEU), Abkhazia and South Ossetia.
- A permissive export procedure for these countries will be approved by a special government decree and relevant ministries.

The decision will be valid until the end of 2022.

Also, **on March 11**, the State Duma [passed](#) in the first reading a draft law to regulate turnover of medicines and medical devices in Russia.

- The draft law allows the Government to establish a special order (until December 31, 2022) for importing registered medicines into Russia in the packaging used for other countries' markets under the condition of full compliance of medicines with Russian regulation and the presence of labeling (sticker) in Russian language.
- Besides, it sets that manufacturer of medical devices cannot suspend or stop in full import of medical devices into Russia without making a prior 6-month notification.

Economic policy and crisis bailout measures

On March 7, the Government resumed targeted support measures for systemically important companies. The term "systemically important" was introduced in 2020 with the onset of the crisis caused by the spread of the coronavirus, the list included large taxpayers and employers. Subsidiaries of a number of foreign companies are also included in the list of backbone companies. The list of support measures includes state guarantees necessary for restructuring loans and obtaining new ones, as well as subsidies for cost recovery.

Also **on March 8**, the Ministry of Finance allowed Russian state-owned companies that fell under the sanctions of states from the list of «unfriendly countries» not to post information about their purchases



on official resources (public procurement website). This measure was taken to protect suppliers of state-owned companies from imposing secondary sanctions for participating in purchases from such companies.

Moreover, **on March 11**, during a meeting of the Government commission on improving the stability of the Russian economy in the face of sanctions, Prime Minister Mikhail Mishustin [announced](#) that companies affected by sanctions would have the right not to publish a list of their counterparties in order to save them from unnecessary risks. Also, customers will be able to write off forfeits, penalties and fines regarding suppliers who cannot fulfill their obligations due to sanctions.

Tax Policy

On 9 March [the law](#) that gives additional powers to the Government in terms of tax benefits for the rest of 2022 was signed by the President. The law provides for the following:

- Possibility to suspend, cancel or postpone tax audits.
- Extension of deadlines for payment of taxes, fees and insurance premiums.
- Extension of deadlines for payment of advance payments for regional and local taxes.
- Extension of deadlines for reporting to the tax authorities.

On March 16, President Putin signed an [executive order](#) on measures to ensure economic stability and protection of the population in the Russian Federation. Among other things, the executive order the leadership of the Russian regions to take the following measures:

- Conduct operational monitoring of retail prices for essential goods, medicines, medical devices and their availability in retail outlets.
- Monitor the situation on the labor market and take measures to support employment.
- Ensure the uninterrupted functioning of life support facilities, transport, logistics, social infrastructure, educational facilities, healthcare, social services, energy, industry and communications.

These measures can potentially affect not only Russian but also foreign companies. In the context of support measures, the President also [signed](#) an executive order on expanding the powers of governors, who will head the so-called headquarters for supporting the economy.

Legislation and Initiatives Being Under Discussion

Risks to assets of foreign investors leaving Russia

On March 10, the Government released more details of a draft law governing the procedure for appointing external administration to foreign companies that have decided to stop their activities in Russia, as well as the criteria for introducing external management.

The draft law initiated by the Government may affect enterprises with a foreign participation share of over 25% (direct or indirect ownership by representatives of "unfriendly countries"). External administration can be introduced in two cases:



1. The termination of the entity's economic activity in Russia ("hard mechanism")
2. Actions of management bodies that may lead to termination of activities, liquidation and bankruptcy, for example, termination of contracts that is important to keep operations, dismissal of more than one third of the staff, etc. ("soft mechanism").

Below are the mechanisms for applying the provisions of the draft law in both cases.

"Hard" mechanism

- The right to apply to the arbitration court with an application for the appointment of an external administration is granted to a member of the Board of Directors or the Federal Tax Service.
- The court takes interim measures to preserve the property and employment of the company.
- The owner (more than 50%) has the right to submit a petition to the court within 5 working days to challenge the appointment of an external administration due to resuming of work or selling of a business. But if an interim administration is appointed, the owner will no longer be able to stop the process.
- If the owner has not submitted a petition, the court appoints an external administration for 3 months. After that, shares of the new organization will be put up for auction by the external administration.
- The buyer is obliged to keep at least 2/3 of the jobs and the continuation of the activities carried out by the organization in the territory of the Russian Federation for at least 1 year.
- The total duration of all procedures is 4 months (*3 months for "rebuilding" and 1 month for sale*).

"Soft" mechanism

- The mechanism is applicable in case management bodies carry out actions that may lead to unjustified termination of activities, liquidation or bankruptcy of the entity.
- An external administration is appointed for 6 months (not for 3).
- Unlike the first mechanism, the process is reversible for an owner.
- The owner (more than 50%) within 6 months has the right to submit a petition to the court to terminate the activities of the external administration with the intention to resume activity or sell the share.
- If the owner has not filed a petition, after 6 months shares of the company are put up for auction.
- The total duration of the procedure is 7 months (*6 months for external administration and "repackaging" assets, 1 month for sale*).

The state development corporation VEB.RF will act as an external administration in all cases except for financial organizations (for them Deposit Insurance Agency will act as the external administration). The main task of the external administration is to prepare assets for sale (inventory of assets, formation of a list of creditors' claims, valuation, etc.).



On March 10, President Putin announced the need to "act decisively in response to the closure of enterprises by foreign owners" and, if necessary, introduce external management. Given Putin's position, the likelihood of the law on "external administration" being passed is high, but this will be preceded by a short but intensive discussion between the advocates of a tougher and softer approach among decision-makers.

Supporters of a softer line include representatives of the business community, as well as a number of representatives of the government's economic bloc. The hardliners are concentrated in the national security and are to some extent supported by First Deputy PM Andrey Belousov as well as a number of MPs.

RSPP and MoED initiatives to soften a draft law in "external administration"

On March 11, the Russian Union of Industrialists and Entrepreneurs (*RSPP*, the biggest Russian business association) published amendments to the draft law "On external administration" (*still officially not submitted to the State Duma*).

The RSPP noticed that measures should take into account the different nature and reasons for suspension of business activity (including public and foreign governments' pressure) and decrease in the investment attractiveness of Russia. The Union proposes the following:

- Increase a foreign participation share from 25% to 50%.
- RSPP suggests that current share does not allow to block the economic activity of the entity and increases risks for Russian entities.
- Introduce the right to postpone the sale of the business of auction and keeping it under the external control for a period of up to 3 years - in order to give foreign investors an opportunity to return.
- Authorize the courts to recognize a part of the company under foreign ownership as non-controlling (*if the Russian co-owners are ready to take over full management*).
- For cases of an objective economic prerequisite for the termination of the business activities (*or in case of firing of more than 1/3 of employees*) external administration will not be appointed.
- The procedure of transferring funds remaining after satisfying creditors' claims in cases of bankruptcy or liquidation of the company must also be fixed.

On March 14, Minister of Economic Development Maxim Reshetnikov announced that a significant part of foreign business, including retail chains, would return to Russia. Reshetnikov linked the decision to suspend work in Russia with logistical problems, thereby shifting the focus from voluntary exit from the market, which may provoke the Russian authorities to harsh measures against such companies. However, Reshetnikov is not a key decision-maker in the economic bloc of the Government (compared to the First Deputy PM Andrei Belousov and some others).

Draft amendments to Criminal Code introducing responsibility for compliance with sanctions in Russia

On March 15, Chairman of the General Council of the United Russia party and First Deputy Chairman of the Federation Council Andrey Turchak proposed to impose criminal liability for companies that comply with sanctions against Russia inside the country.



According to the statement, the United Russia party proposes to prosecute for compliance with Western sanctions in Russia. This measure is a reaction to cases when Russian companies (*including state-affiliated*) refuse to work with sanctioned banks and enterprises because of the risk of being sanctioned.

Please note that the draft law imposing criminal liability for compliance with sanctions was already discussed in 2018 but put on hold under significant pressure from largest Russian companies and banks.

Currently, the probability of its adoption seems much higher, although it is not yet a consensus. The probability of adopting the law will increase if the Government, the Prosecutor General's Office and the Supreme Court support Turchak's initiative (according to some reports, the draft law was prepared and currently sent to these bodies).

Official submission is only possible based on the above-mentioned opinions, date of submission is thus unclear and the wording / scope of enforcement can change.

Import regulation

During the discussion in the Federation Council (upper house of parliament) of the law on mechanisms to support the sustainability of economic development under sanctions, a statement was made on the legalization of parallel imports (import of goods of original goods without the permission of the copyright holder and usually through third countries). Senator from St. Petersburg Andrey Kutepov announced that "parallel imports are being legalized by exempting from liability those who import and sell goods from the list determined by the Government."

Thus, the mechanisms applied to intellectual property products can be extended to listed goods (to be developed by the Government) of foreign companies. The possibility of parallel imports is likely to be provided for by separate regulations (government decree) in the near future, developing the provisions of the adopted law.

On March 15, Maxim Topilin, Head of the State Duma Economic Policy Committee, reported on the preparation of the relevant Government decree. In particular, Topilin said that some parallel import schemes will affect the pharmaceutical market.

On March 15, PM Mikhail Mishustin during a meeting of the Government Commission on improving the sustainability of the Russian economy announced a number of measures to support imports, including:

- Russia will suggest EAEU member-states to increase the customs duties threshold for cross-border e-commerce from EUR 200 to EUR 1000 until October 2022.
- It is also proposed to fix the exchange rate when paying import duties; establish priority for consumer goods during customs clearance (primarily for food and medicine); simplify customs clearance procedures and zero customs duties for the list of critical import goods (to be formed).

The Government plans to implement these measures by the end of March.



Price regulation

A draft law to introduce price regulation for food products, medicines, goods for children, household chemicals, etc., has also been drafted by line State Duma committees. The draft law has not been officially submitted to the State Duma.

On March 16, the head of the Committee on Industry and Trade of the State Duma, Vladimir Gutenev, proposed introducing state regulation of prices for gasoline and diesel fuel, sending the respective suggestion to the government. According to the initiative, during the period of sanctions, the Government will be able to set marginal wholesale and retail fuel prices, since the cost of socially significant goods and products depends on them.

The introduction of direct price regulation (setting marginal prices) for fuel could become a precedent. In the future, it can be extended to other significant goods (food, medicines, building materials, etc.).

At the moment, the Government is developing tools for softer price regulation. Thus, **on March 14**, it became known that the Ministry of Industrial Policy and Trade proposes to temporarily “untie” prices for metallurgical products and raw materials from the dollar exchange rate, setting the maximum possible prices for certain types of goods on the domestic market. A [draft resolution](#) was prepared allowing the ministry to conclude price agreements with manufacturers and sellers of these goods until the end of 2022. It should be noted that in 2020, similar price stabilization agreements were signed with retailers for sugar and sunflower oil.

Public Comments and Discussions

The discussion about a possibility to freeze or even confiscate the Russian assets of companies from the US and EU jurisdictions erupted, with a number of opinions from more moderate to more radical stated by various stakeholders:

- **On Feb. 27**, former President of Russia and currently Deputy Head of the Security Council Dmitry Medvedev stated that Russian could confiscate and nationalize assets of companies from jurisdictions which imposed sanctions. Probably, Medvedev voiced the most radical scenario among a number of options being considered.
- **On March 1**, Prime Minister Mikhail Mishustin made a statement regarding the prospects for the presence of foreign investors in Russia. He confirmed that the Government "considers foreign businesses as potential partners" and is open to dialogue with constructive investors. “Those who will not curtail their projects will win” in Russia, Mishustin said. Thereby, the Government sends a message that keeping deeply rooted foreign companies in Russia is desirable, especially the companies in the consumer sector (to contain prices and prevent shortages).

A general framework of the Russian approach to foreign investors and their assets in Russia was stated on March 4 by First Deputy PM Andrey Belousov during the meeting with the Russian business community. His remarks outlined one of three options the Government will act in relation to foreign investors. They represent the Government’s attempt to at least delay a massive outflow of FDI from Russia. Belousov mentioned 3 options for interaction with foreign investors: 1. *business continuity* 2. *transferring a stake to Russian partners for management* 3. *fast-track bankruptcy*. The External



Administration draft law provides the legislative framework for the third option. In the near future, it is expected legislative initiatives encouraging foreign companies to remain in the Russian market.

On March 10, Andrey Klishas, Chairman of the Committee on Constitutional Legislation of the Federation Council, stated that “in relation to foreign companies from unfriendly countries that leave Russia, not only such measures as nationalization, but also restriction of property rights, a ban on voting by blocks of shares can be applied. in subsidiaries, blocking assets and other measures.” Klishas' statement reflects the authorities' search for various options for influencing foreign companies, depending on the nature of their behavior on the Russian market (from softer to tougher measures up to nationalization).

On March 10, during a meeting with members of the Government, President Putin made a number of statements regarding the possibility of limiting the export of Russian goods that are critical for many Western countries, including grain and potash fertilizers. The reason for such restrictions may be the need to prevent a shortage (rising prices) of food in Russia itself.

On March 11, the Prosecutor General's Office of the Russian Federation Igor Krasnov instructed to strengthen supervision over compliance with the law by foreign companies that announced the suspension of activities in Russia. We are talking about tighter control over compliance with labor laws, fulfillment of obligations to contractors and obligations to the state.

On March 11, the Prosecutor General's Office appealed to Roskomnadzor with a request to restrict access to Instagram in connection with the changes in the Company's hate speech policy removing the restrictions on calls to commit violence against Russian military personnel in Ukraine. The Prosecutor General's Office also applied to the court to designate the Meta Platform, which owns Facebook, Instagram and the WhatsApp, as an extremist organization. The appeal is made with regard to changes in the policy of social networks, leading (according to the Prosecutor General's Office) to inciting hatred against Russian citizens. The appeal may result in a complete ban on the activities of Meta Platforms in Russia.

We will closely monitor next steps around these initiatives.

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If you would like to schedule a discussion of this paper and learn more details about the above listed documents, please contact Yury Panasik, Partner, y.panasik@kesarev.com



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